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East German economic planning and price reform under the new economic system.

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East Germany/Soviet BlocEconomic/politicalEast German comments on economic planning and price reform

(July 1964)

~~4~~ During discussions about economic planning and price reform, senior East German economists and officials made comments as follows :

(a) The economic planning system of the D.D.R. is still under discussion and final decisions have not yet been taken. The new system will not represent a sudden change but will be an evolutionary stage. The VI Congress of the S.E.D. in January - February 1963 decided that a new system could be introduced because productive socialist relations had been attained and a firm state frontier had been established. (The open border had caused a loss of 30 billion D. marks.)

The first economic plan, in 1948, was based on the Soviet model, but it took years to train a planning staff. The new system is more complex - no one aspect should be seen in isolation - and there are four main lines of reform, the first three being the introduction of scientific methods into planning, the development of central planning techniques, and the development of incentives.

On the first point the essential is the definition of levels of responsibility. The new associations (VVB) are in principle on a product basis, e.g. the main footwear plants are in one VVB but small plants are outside. There are three territorial VVB's for coal but normally they are country-wide for a single product. The VVB is not responsible for private or half-state enterprises unless they are particularly important. The Deutsche Investbank or the district branches of the Deutsche Notenbank hold the state shares in half-state enterprises but voting rights are exercised by a VEB in the same sector. The new feature is that the VVB is responsible for one group of products, including local industry. Technical development and balances are now transferred to the VVB from the central organ. [redacted] 50X1-HUM

[redacted] Management research and information techniques are to be developed, including the operations research of capitalist enterprises (which we previously rejected). Centralism has been too bureaucratic. All short-term decisions will be taken by the VVB and only long-term structural changes will be left to the central organs. 50X1-HUM

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Secondly the development of central management is to be put on a scientific basis. We want to introduce long-term planning for technical development. We used to set up 5 and 6 year plans but could not forecast technical progress. We now try to foresee technical progress for 10 or 15 years ahead, i.e. the level that other countries will reach by those dates. This cannot be done in detail and the prognosis can vary - it is essentially "a fantasy based on exact facts". We may forecast technologies but cannot know how far they can be translated into economic terms or which of them should be used in the D.D.R. We can only get a "raw outline" of the future.

Unlike long-term plans, the 7-year plan (1964 - 1970) can be better optimised. We identify technical progress, import and export efficiency and evolution of the structure of consumption. Hitherto planning was effectively co-ordinated only annually and the 5 or 6 year plans were not effective in this respect. The new system co-ordinates at the longer term level with annual plans as executive program At the same time new 50X1-HUM experience must be taken into account in the long-term plan which must be revised continuously.

Long-term plans are the responsibility of the central plan agencies but not in isolation from the executants. Long-term plan commissions have been set up with VVB participation. These planning groups are responsible for forecasting technical progress in their sector and for each group of products. In the Volkswirtschaftsrat (VWR) there is, say, a textiles, clothing and leather department, which has VVB's, as does the Landwirtschaftsrat (LdWR), the Ministry of Foreign Trade, the Transport Ministry, etc. The State Planning Commission has departments analogous to those in the VWR as a co-ordination centre for the entire economy. The executive level of authority runs up to the VWR but the State Planning Commission is a working agency of the Council of Ministers, like the Committee for Research not exercising executi 50X1-HUM authority. The VVB's are responsible for carrying out plans and laying out the detail. They set out general proposals on technical progress, consumption needs and export prospects. The plan itself is evolved in interchange between the State Planning Commission and the executive levels.

We are now working on new balance techniques requiring electronic computers for solution. Plan balancing is the most crucial part of the plan and has in the past been done with punch-cards and small calculating machines. It was both incomplete and over-detailed. A 27 X 27 input/output table was published but no larger one in the D.D.R. so far. The input/output table must have better primary documentation. Our 27 X 27 table was an experiment, aimed at balancing gross production. The basis was production sold by factories, whereas the Soviet input/output table

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was based on existing statistical data, not on specially collected data. This practice has limits but the big difficulty is the information system. After trials we made an ex ante input/output table for 1964 which was ready at the same time as the 1964 plan prepared by traditional methods. It was simply used to check the 1964 plan. But seeing the input/output table the Council of Ministers required that every annual plan should include an ex ante input/output table. But in our system balances in groups of products are worked out by the administrative user whereas the input/output table reflects the technological process. We need two tables, item by item (the LEONTIEFF-type) called the principle of groups of products, and the office by office or the principle of administration. The latter is on a sales only basis whereas the former is on a production basis.

The Volkskammer has to adopt the Plan and Budget at the same time so co-ordination is essential between production and financial flows. There is, however, often a failure to fulfil the capacity commissioning plan while the investment outlay plan is fulfilled. Enterprises have purchasing power when the goods for that money are not available. There is not yet complete co-ordination between the financial and production sides.

In the first stage of development production is most important, but in the second stage [] consumer preferences, limits of resources, all summed up in price, must be more deeply studied. In its incentive aspects the new system would be impossible without planning of price and purchasing power.

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Trade outlines are the responsibility of the State Planning Commission and the Ministry of Foreign Trade, using the research of the foreign trade corporations and VVB proposals. The foreign trade plan forms part of the overall plan, co-ordinated with the investment plan and foreign policy requirements. Foreign Trade enterprises and VVB's give these concrete form. The new economic system involves a change as import/export corporations for [] groups are now changed to "real enterprises", i.e. working on cost accounting to maintain profitability just like any other enterprise. They co-ordinate with VVB's. The corporation buys from the VVB at domestic prices and the valuta D.M. is a fictitious transaction, in transferable roubles or dollars. They must be profitable on domestic prices but they also have a foreign currency plan. Their profit is solely in domestic values and the new price system is hence the crucial problem. Co-ordination within C.M.E.A. is carried on at all levels of planning. Every East European long-term plan must start from energy (power) planning. Hence intra-C.M.E.A.

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planning must start with the drawing-up of an energy (power) balance. Attached at Appendix "A" is a tabulation of authorities for composing balances.

(b) The price reform is in three stages. April and July reforms are the first stage and covered materials. The second stage will cover engineering and the third all other goods and they will be completed by 1966 although exact dates have not been fixed. The principle of the reform is that under normal conditions every enterprise must break even. Prices will allow "normally-run" enterprises to keep running. Raw material reforms were therefore the start. Subsidies allowing abnormality will in time be withdrawn. The long term plan lays down supply of equipment but not all loss-implicit equipment will be replaced by 1970. The problem is to shut obsolete plants and replace equipment.

Account has to be taken of limited raw materials supplies. We have to use capacity to the utmost. Thus to produce sulphuric acid we have to continue to use lead-chamber methods though they are dearer than anhydrides. At present all production capacity is required to meet demand but only those making profits will be expanded.

In the present price-reform there was no capital-use charge but only capital demand. When fixing prices we took into account the need for new plant as prices must cover investment needs. Factories would be forced to use capital better if a charge were levied but this is still under discussion. If the rate of interest can allocate capital better it should be on the lines of a high rate such as Bulgaria's 15% and as a pay-back period. We are calculating these as an experiment, from 1st July. From 1st January 1964, VVB's must work on autonomous finance. They were responsible for running enterprises but they are now partners in the enterprise.

Our imports pricing is relatively easy. We base it on foreign trade plus transport costs. Thus export industries working on imported raw materials have full cost basis. Everything is included in import prices which thus reflect world market capital intensity in raw materials. But we do not measure capital intensity in manufacturing because we do not reflect foreign prices at this level. World market prices can only be compared on an international basis

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Import prices are based on world market prices and goods produced at home on a "mixed basis". The trend for the future will be to bring export prices to the world market. There are at present "treaty prices" - the costs of the biggest C.M.E.A. producer. C.M.E.A. is researching on

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the basis that all socialist country costs are covered, not on the basis of any one country's costs but on that of the average of all C.M.E.A. production. But no decision on a C.M.E.A. "own price basis" has yet been reached. Prices for flow-of-funds analysis are still embryonic.

Turnover tax or production levy, for which the rates were laid down in 1950-55, was intended to equalise profits on individual products. But costs have changed. In the new price reform new raw material and machinery prices mean that no enterprise is inhibited from production by below-cost prices. Retail price changes in the future cannot be judged from prices of producer goods. For consumer goods the aim of the reform is to reveal real cost prices but this stage has not been reached. The turnover tax in consumer goods has been cut to take account of the increase in the price of raw materials by 1st April 1964. Some flexibility is now envisaged for turnover tax. As long as the reserves of the national economy against inflationary pressure are small we must be cautious about changes. At present we are mainly concerned to prevent price rises for raw materials being passed on to the retail consumer. All prices are in principle laid down by law and enterprises must apply for a new price.

Price zoning is as a rule not applicable to consumer goods, except for coal which varies by coal mine. For producer goods there are prices franco ex works station. Transport is not so important in the D.D.R. The sales price allows for average transport costs. We are interested in West European price formation on integration.

(c) The new measures can only become effective because the state frontier has been closed. Until 1961 administrative measures were directed solely at problems arising from the open frontier. We now want to move from administrative to economic levers.

The State Planning Commission gives main directives to the VWR for industry. Each industry section has a number of VVB's. There are now 250 economic indicators in the annual state plan and we want to reduce them. Under perspective planning the settling of long-term targets for the VVB permits the reduction of indicators in the Annual plan. The enterprise has to pass its plan indicators upwards rather than downwards. The VVB has been changed from an administrative entity to a planning and financially independent agency with responsibility for plan fulfilment. The kind of plan indicators given by the VVB's is goods sold, technical progress, production costs of new groups of products - all the traditional ones except gross production. Foreign trade corporations are supposed to work more closely with enterprises and VVB's though the calculations are in DM prices. As an experiment the Ministry of Foreign Trade is trying to transfer some of its corporations to the VVB's. Thus the D.D.R.

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will supply over 100 chemicals plants to the U.S.S.R. by 1970 : the VVB's are directly responsible for supplying and installing this equipment. Practical necessity requires this to be extended to the capitalist market.

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The WB has a technology fund as a levy on its enterprises for research. Another fund is a profit pool for all its enterprises. And thirdly there is a premium fund for intra-VVB competition. This premium fund comes from the profits of enterprises at a fixed scale. A "treaty" is concluded between VVB and factory, settling a given task (e.g. production of a given article by a given date) and offering a premium if the task is fulfilled.

The factory director may get up to 5,000 DM for the fulfilment of special tasks under this "treaty" system but the premia are mainly for the enterprise staff. The "treaty" lays down who are the key staff to get premia - the drafting staff, the specific workshop brigade, etc. Their names are laid down in the "treaty". It is now laid down that up to 30% of salary should be bonus under the premium system. The new system decrees that only 70% of basic salary is payable in any event. The other 30% is paid when plan indicators are fulfilled, paid out of the enterprise wage fund. When the plan is over-fulfilled an extra premium is payable.

Fixed assets have just been revealed for 1963 and have been written into the books of enterprises on 1st January 1964. The revaluation of assets and the new price reform are the crucial features of the new economic system. Prices have to be fixed on a cost basis. The system is introduced step by step so that each step can be carefully assessed. At all costs it must not lead to a rise on the retail market. The shortfalls shown by the revaluation of assets will be carried on the budget.

The former premium system which has been replaced by the 3-tier system was a single fund, $4\frac{1}{2}\%$ of wage fund, payable out of profits and divided into two sections. About one third of the $4\frac{1}{2}\%$ was always paid. Formerly the establishment of the premium was essentially gross production. Now in 1964 the April and July price reforms allow attention to profit change : in 1965 engineering prices will be reviewed and the whole reform will come later.

Gross production productivity and cost reduction were the former premium criteria. But an enterprise could simulate gross

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production output by using input goods. This was stopped on 1st January 1964 : until then gross production determined the premium, with reductions if productivity and cost of production plans were fulfilled, viz. a reduction for each $\frac{1}{2}\%$ underfulfilment. The higher the overfulfilment the higher the premium and a sufficient overfulfilment of the gross production plan could offset underfulfilment in the other two indicators. The new premium indicators are generally productivity, production cost, assortment, production of new items, quality indicators, sales or exports. Now the profit plan is the main indicator, plus exports, commercial production and technical progress. All plants must have these four indicators plus one or two others from the previous list.

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(d) VEB BERLINER WERKZEUGMASCHINEN FABRIK, of which the KAERGER factory was the original nucleus, employs about 2,000 staff. Three quarters of its output are new models, covering grinding and abrasives and automatic lathes. There is no intra-enterprise cost accounting since this is best adapted to clearly defined shops. We divide our work into small mechanical operations, large mechanical operations, assembly and finishing. All three groups work for the same end-product. Each is given quarterly and monthly plan indicators. There are basic material inputs, cost indicators for various processes, breaking down wages and waste products. This indicates the value of materials used. Price ratification by the Price Office is effected by technical coefficients and a check on factory book-keeping. This is not the responsibility of the VVB. As the enterprise works mostly on exports the price limits are laid down by contract, negotiated through the Engineering Export Agency, but the enterprise can look for its own markets. Indeed this direct link with customers must increase both at the VVB and enterprise level, just as ZEISS have direct customer relations.

We do not use the foreign trade price in the factory, as in Poland and Hungary, but we may be forced to buy materials from high cost D.D.R. plants. Such a calculation would be academic as we have no influence over and cannot choose our suppliers.

Being under construction the enterprise is not yet profitable : at present it is not subject to the production fund levy. We have revealed our assets and this has affected our cost prices through depreciation. We are paying more for power and foundry products. Our prices cannot be raised though in the price reform the prices of precision machine tools will be raised, and for very special machines under development may be raised 8 times over : but this is offset by the very high productivity of the machine. The aim of the price reform is to transfer the possibility of accumulation to the basic industries which have hitherto had to be subsidised.

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As plan indicators the enterprise gets : goods production, quality indicators, production cost reduction, research and profit plan. Everything is also drafted in the internal plan : production plan and new technology, social measures, finance are written into the annual technical economic plan, submitted and approved with the VVB. This is then confirmed in the autumn. The practice of quarterly and monthly planning has been abandoned but the VVB management controls special tasks.

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